TESTIMONY OF JOHN F. LOGAN
AUTOMATION GROUP PRESIDENT
DT INDUSTRIES
CHAIRMAN
AMT – THE ASSOCIATION FOR MANUFACTURING TECHNOLOGY
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I. INTRODUCTION

My name is John F. Logan. DT Industries (DTI) is a leading global and the largest North American provider of automated assembly, test, material handling and packaging systems for a broad range of consumer and industrial products. DTI consists of two complementary operating groups – Automation and Packaging. I am President of the Automation Group. The Groups, and the divisions within them, share design, engineering and manufacturing resources in pursuit of indispensable engineered solutions for customers delivering local service within the context of global teamwork. DTI provides our engineering and manufacturing expertise to customers involved in electronics, automotive, pharmaceuticals, consumer products, high technology, medical devices, cosmetics, hardware, agriculture and heavy trucks.

DTI currently operates 20 manufacturing facilities located in the United States, the United Kingdom, Canada and Germany. Additionally, we have an extensive service network established in over 15 countries. We employ approximately 2,800 people.

I am Chairman of the Board of Directors of AMT – The Association For Manufacturing Technology — a trade association whose membership represents over 370 machine tool building firms with locations throughout the United States, including DT Industries.

The majority of AMT's members are small businesses. According to the U.S. Census of

Manufacturers, 73 percent of the companies in our industry have less than 50 employees. They build and provide to a wide range of industries the tools of manufacturing technology including cutting, grinding, forming and assembly machines, as well as inspection and measuring machines, and automated manufacturing systems.

- **THE U.S. MACHINE TOOL INDUSTRY IS CRITICAL TO OUR NATIONAL AND ECONOMIC SECURITY**

The United States machine tool industry is critical to both national security and economic prosperity. With production of over $7 billion, the machine tool industry is small when compared to other industries. But that industry's products and technology are the essence of the industrial manufacturing process and the key to a strong defense industrial base. Without the manufacturing technologies related to machine tools, the other manufacturing industries would not exist. With 377 members, AMT-the Association for Manufacturing Technology represents the U.S. machine tool industry, comprised of companies that provide manufacturing technology to cut, shape, form, and assemble metal and other materials and provide software and measuring devices for those processes.

By definition, machine tools and related manufacturing technology are the "tools" of production. Our nation's ability to compete globally in electronics, optics, aerospace, and other high technology arenas and our ability to produce advanced weapons systems for national defense depend on the availability of state-of-the-art machine tools and the health of the U.S industry. Without machine tools and related manufacturing technology there would be no aircraft, ships, tanks, or missiles. Nor would there be appliances, automobiles, agricultural machines, or factory automation without machine tools. In short, life as we know it today would be impossible without the modern machine tool industry and the manufacturing technology related to it.

The industry was a serious bottleneck to military production during World Wars I and II and the

Korean War. Even during the Gulf War, the need for production increases in specific weapons and mobilization priorities pushed civilian manufacturing projects to the back of the production queue so that weapons systems and war materiel would be available in a timely fashion for the conflict with the Iraqis. Indeed, throughout our history machine tools have been a critical tool for mobilization and eventual victory over all the enemies we have faced. That is even more true today given the high-tech nature of America's weapons systems, than when machine tools were used to make the rifles and cannons of the Civil War.

Wartime production priorities and mobilization require large numbers of machine tools be made available on short notice, and that can only be accomplished with great assurance by a strong and healthy domestic machine tool industry. While the U.S. Government, using laws such as the Defense Production Act, can order machine tool production to be converted from civilian to military priority as soon as the need arises, the U.S. Government cannot order foreign machine tool makers to do likewise. It can only make a request, and then hope that our allies see a particular conflict in the same way that we do. Certainly, there is no guarantee that our European or Asian allies will see every conflict from the same perspective as the United States. Moreover, despite our current overwhelming military dominance, air and shipping lanes are not as secure in wartime as they are in peacetime. That is why the U.S. defense industrial base is only considered by the Pentagon to include the continental United States, plus Mexico and Canada.

Machine tools play an equally important role in peacetime as well. Machine tools are the heart of our civilian economy and, hence, our prosperity. Alan Greenspan has testified before Congress to the fact that U.S. corporate profits and worker wages have risen dramatically without inflation in recent years in large part because productivity is once more on the rise. A good part of that productivity can

be traced back to the effective use of more efficient machinery and factory automation. In essence, Chairman Greenspan was explaining that the output of the modern U.S. machine tool industry accounts for a good deal of our recent spurt in productivity and, hence, has played an important role in our current prosperity.

If we were to lose the domestic core of our machine tool industry, we would become wholly dependent on our allies and trade competitors for the industrial production machinery that fuels our productivity and our keeps our industries on the cutting edge of the latest technology. Without a domestic base for machine tools, Boeing would be second in line behind Airbus; and General Motors and Ford would have to wait behind Toyota before acquiring the latest in production equipment. Being second to market with innovation is not the way to maintain industrial leadership. That is not a situation in which we should want to place our key industrial sectors, which is why a healthy domestic machine tool industry is so important both for national security and for continued prosperity.

The recent combination of a sharp decrease in U.S. demand and a huge increase in Asian exports to the U.S. marketplace has been extremely damaging to the U.S. machine tool industry.

III. THE MACHINE TOOL INDUSTRY DOWNTURN (1998-1999)

Over the past year, domestic demand for machine tools has fallen dramatically. The first six months of 1999 have seen machine tool consumption in the United States fall 39 percent when compared to the same period last year (see Chart 1). While all but a handful of machine tool product areas experienced lower order rates in the first half of 1999, some product areas were severely hit (see Chart 2). Machine tool consumption has traditionally been used by economic forecasters as a leading indicator of the larger economy. Whether the decline is a harbinger of an overall slowdown from what has been an amazing record of economic expansion; or whether it is an indication of structural changes

in traditional capital spending patterns; or is a combination of these factors; the sharp decline in U.S. machine tool consumption should concern thoughtful policy makers.

The U.S. machine tool market is composed of manufactured durables producers - the largest of which are the auto parts industry, Detroit's Big Three, the aerospace industry, and the off-road and highway construction industry. Total capital spending (including machine tools) for these four sectors fell 21 percent during the first quarter of 1999 relative to the first quarter of 1998, although the spending levels varied significantly by sector. The auto parts industry's capital spending climbed 45 percent while capital spending by the aerospace industry and Big Three both fell by 25 percent. The 39 percent decline in machine orders cannot be accounted for solely by these significant capital spending declines among the major customers.

Some Wall Street analysts suggest that some of the difference can be attributed to a significant change in the mix of capital spending in 1999 relative to the mix over the past three years. In the past three years, these four sectors spent heavily on new manufacturing technologies and increases in capacity to meet the growing demand of the world market. In 1999, capital spending will be focused more towards software solutions to the Y2K issue and investments in knowledge and information technologies. The Y2K issue is a short-term distortion whose impact will dissipate over the next twelve months. The shift from investments in new capital equipment is a longer-term issue.

Many financial analysts point to lax bank regulation and extraordinary investment in new capacity during 1994-1997 by Asian auto, auto parts, and heavy equipment manufacturers as principal causes for the financial crisis in Korea and other Asian countries. Economists who follow the situation in Asia suggest that it may take two to five years to rationalize the over-capacity in various industries throughout Asia. In the meantime, additional capacity needs of the U.S. auto and heavy equipment

industries will be weighed against the cost of investing/buying foreign capacity in Asia at fire sale prices.

Not only is the U.S. machine tool market three-fifths of the size that it was at the end of 1997; but to make matters worse, this already vexing problem has been compounded by a sudden change in the marketing approach and an increase in the market share of the three largest Asian producers of machine tools: Japan, South Korea, and Taiwan. In addition, U.S. machine tool exports to Asia have collapsed (e.g., machine tool exports to Korea dropped 69 percent from 1996-1998).

Their approach has utilized a very aggressive – if not predatory -- marketing strategy that has seen, even accounting for currency fluctuations, Asian prices for some commodity machines cut 50 percent or more in just one year (see Chart 3). As a result, Asian machine tool builders have increased their shares of the U.S. market to the point where U.S. builders have seen their domestic market share decline over the past year to a level where we now supply about 40 percent of the U.S. machine tool market, compared with about 50 percent or more a few years ago (see Chart 4). AMT does not have legal standing to initiate an antidumping case on behalf of its members.

The import surge from Asia can be explained by the Asian financial crisis, brought on in part by over-investment in certain key industries, including machine tools. But whatever the cause, the response chosen by the Asian machine tool builders to the lack of demand in the Asian marketplace has been to export their over-capacity to the United States. One telling example of the shift caused by the Asian financial crisis is that South Korea, which only exported 15 percent of its machine tool production to the United States in 1995, exported fully 50 percent of that production to the U.S. in 1998. Similar, if less dramatic, shifts have occurred in Japan's and Taiwan's exporting patterns (see Chart 5).

The dramatic decline in U.S. machine tool industry orders over the first half of 1999 can be attributed to a decline in customer demand and a significant increase in import competition. Both can be

directly related to the effects of the Asian financial crisis, which has also had a substantial negative impact on U.S. machine tool exports to Asia.

During the past 13 years, two Presidents have seen fit to negotiate Voluntary Restraint Arrangements ("VRAs") with Asian Governments; because they concluded that the continuation of a healthy U.S. machine tool industry was critical to national security. Those VRAs lasted seven years, during which time the industry did exactly what was required to return to profitability and competitiveness. U.S. machine tool builders doubled their investment to depreciation ratios. They dramatically increased expenditures on research and development, and by the termination of the VRAs in 1993, U.S. machine tool competitiveness in world markets was measured by the fact that the industry was actually exporting over 30 percent of its output.

Nonetheless, the recent combination of a sharp decrease in U.S. demand and a huge increase in Asian exports to the U.S. marketplace has been extremely damaging to the U.S. machine tool industry.

IV. WHAT SHOULD BE DONE TO HELP THE U.S. MACHINE TOOL INDUSTRY

Given the importance of the U.S. machine tool industry to America's national and economic security, the U.S. government must adopt policies that assure the continued strength of America's machine tool industry and which provide a level playing field for American machine tool builders. These actions include:

- Enactment of an 18-year product liability statute-of-repose.
- Vigorous enforcement of U.S. trade laws – both to assure that trade is fair and that the national security is protected.
- Passage of tax laws that encourage U.S. manufacturing and that are saver/investor friendly.
- Adoption of technology/R&D policy and funding that assures that U.S. manufacturing technology is second to none..

- Application of sensible export control policy and regulations.

I would like to say a few words about our current export control policy. Mr. Danjczek will address the issue in greater detail. However, I want to describe what I saw at the China International Machine Tool Show last week. Several Chinese companies were showing fully integrated 5-axis CNC-controlled machines. In addition, several are showing very high accuracy turning and milling machines with accuracies of +/- 3 microns and one spherical lathe with accuracies of +/- 2 microns. These are machines that U.S. manufacturers cannot export to China because they are considered a national security threat in the hands of the Chinese. Yet, there they were right on the show floor in China. I will tell you that the unilateral imposition of export controls on machines that are readily available elsewhere is hurting our industry in this critical market without affecting one iota access of the Chinese to the manufacturing equipment they need.

- **FSC REPLACEMENT**

Mr. Chairman, my colleagues will be discussing a variety of other issues which affect U.S. machine tool manufacturers – from product liability to technology policy to trade policy and export control reform. I would like to touch on one other issue before I conclude my remarks – Foreign Sales Corporations. Specifically what does Congress intend to do in the wake of the World Trade Organization's (WTO) dispute resolution panel ruling that the Foreign Sales Corporation (FSC) violates WTO rules and must be repealed by October 2000?

FSCs provide an enhancement to exports by allowing U.S. companies to deduct 14 percent of their export income. These funds are used to make U.S. exports more competitive in world markets. DT Industries has a FSC, as do many other AMT members –both large and small.

Unless Congress acts by October of next year, billions of dollars of U.S. exports will be subject

to retaliatory "compensation" by the European Union and others. But simply repealing the FSC would deprive U.S. companies of a powerful incentive to export and effectively amount to a $3 billion per year tax increase on U.S. exports. On the other hand, simply replacing FSC with a slightly different version could be inconsistent with the WTO decision and could lead to European retaliation.

The dispute resolution panel has pointed the way towards a logical solution to FSC replacement. The U.S. currently maintains a system of worldwide taxation of its businesses. We are the only major industrial nation that does so. The WTO dispute resolution panel clearly states that we cannot couple territorial treatment of exports with a system of taxing the worldwide income of our companies. The solution is to move to a territorial, border-adjustable system of taxation, which would not tax exports at all but would impose a tax on imports. This is the system used by all of our major trading partners.

You may recall that a few years ago, your colleagues, Sens. Domenici (R-NM) and Nunn (D-GA), introduced a comprehensive tax reform proposal called the USA Tax. It called for replacing our current tax system with a cash flow tax that would be both border-adjustable and territorial and would provide for the expensing of capital purchases. Cong. English (R-PA) has introduced similar legislation in the House. AMT supports Cong. English's proposal. Enactment of this approach is a top legislative priority for AMT.

- **CONCLUSION**

We cannot maintain our leadership as either the pre-eminent world power or as the premier world economy with a second-rate machine tool industry. Please listen carefully as my colleagues present their ideas for meeting the challenges facing our industry.